IN THE

Supreme Court of the United States

October Term, 1946

No. 1239

S. L. HURT,

Petitioner,

versus

COTTON STATES FERTILIZER COMPANY *et al.*,

Respondents,

(District Court No. 301)

S. L. HURT,

Petitioner,

versus

COTTON STATES FERTILIZER COMPANY *et al.*,

Respondents.

(District Court No. 316)

S. L. HURT *et al.*,

Petitioner,

versus

FRAMPTON E. ELLIS, as Administrator de Bonis Non Cum Testamento Annexo of the Estate of Joel Hurt, Sr., Deceased, *et al.*,

Respondents.

(District Court No. 324)

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE FIFTH CIRCUIT

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PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE FIFTH CIRCUIT[1]

Your petitioner, S. L. Hurt, respectfully prays that a writ of certiorari issue to review the judgment of the

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[1] It is believed that the argument in support of the petitioner's contentions is sufficiently set out in the Reasons Relied on for Granting the Writ, pp. 20 to 31, *infra*. Accordingly, no separate brief is being filed.

Circuit Court of Appeals for the Fifth Circuit rendered January 3, 1947 (R. 2602, v. V), which affirmed and remanded with directions the judgment of the District Court in No. 301 dismissing your petitioner's complaint on the merits (R. 1955, v. III), affirmed the judgment in No. 316 dismissing your petitioner's complaint upon the merits (R. 2055, v. IV), and affirmed the judgment in No. 324 against your petitioner and in favor of the respondents Ellis and Mrs. Willie Martin Hurt as prayed in said respondents' complaint (R. 2551, 2555, v. V).

No. 301 is a derivative stockholder's suit. It was brought by petitioner as beneficial owner under his late father's Will, and as legal owner through subsequent purchase, of shares of stock of Cotton States Fertilizer Company, a Georgia corporation. Petitioner's status to sue was established on a prior appeal.[2]

No. 316 is a similar suit by petitioner as owner by purchase of further shares of the company.

No. 324 is a suit by respondent Ellis as administrator *de bonis non c.t.a.* of the decedent estate referred to above, and respondent Willie Martin Hurt as an alleged creditor of the said estate, as co-plaintiffs, against petitioner as defendant, for a determination that Ellis, as administrator, is owner of the shares of preferred stock claimed by petitioner in No. 301, and that the co-plaintiff, Willie Martin Hurt, is a creditor of the said estate to such an amount that petitioner has no equity in the said shares and is, therefore, without status to sue.

The writ is sought as against all the respondents, except Messrs. Bloch and Hall in No. 316.

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[2] *Hurt* v. *Cotton States Fertilizer Company*, 145 F. 2d, 293, *cert. den.* 324 U. S. 844.

Jurisdiction

The judgment of the Circuit Court of Appeals was rendered January 3, 1947. Rehearing was denied by order entered January 31, 1947 (R. 2611, v. V). The jurisdiction of the District Court is founded on diverse citizenship. The jurisdiction of this Court rests upon §240(a) of the Judicial Code as amended by the Act of February 13, 1925 [Title 28 U. S. C. §347(a)].

Opinions Below

The opinion of the Circuit Court of Appeals is reported in 159 F. 2d 52 (also printed R. 2588, v. V). Its opinion on a prior appeal in No. 301 is reported in 145 F. 2d 293, cert. den. 324 U. S. 844. The District Court rendered no opinion upon either occasion. Its Findings and Conclusions in No. 301 appear at R. 1930, v. III; in No. 316 at R. 2052, v. IV; and in No. 324 at R. 2537, v. V.

Questions Presented

1. Whether, in a diversity jurisdiction suit, the Federal courts in Georgia were free to decide without reference to Georgia law that there was nothing illegal, fraudulent, or otherwise exceptionable in the following transactions between Cotton States Fertilizer Company, a Georgia corporation, and certain of its officers and directors:

a. **A transaction in which the three officers and** directors of Cotton States caused the corporation to satisfy $49,102.68 of undisputed debts owing to it by one of the directors and a company in which he was interested, upon payment of a part of the consideration to Cotton States and a part of it to the other two directors—it being undisputed that the two directors to whom the part was diverted paid Cotton States nothing for it?

b. A transaction in which the officers and directors of Cotton States caused the company to satisfy $18,352.75 of undisputed indebtedness owing to it by one of the directors, in consideration of his surrendering to Cotton States shares of its common stock at a time when the company was admittedly insolvent and the said shares were worthless?

c. A transaction, carried out at a time when Cotton States was solvent and prospering and its stock was valuable, in which two of the company's officers and directors purchased on its behalf debts owing by it together with shares of its common and preferred stock, but so manipulated the transaction that for $15.22 they got secretly and still retain the stock thus purchased, which included the controlling common stock (607⅔ shares out of 1035⅓ issued and outstanding)?

d. A course of practice over a period of years under which Cotton States' officers and directors used up the company's distributable profit by paying it to themselves as salary increases and bonuses?

2. Whether, in such a suit, the Federal courts in Georgia were free to decide without reference to Georgia law that recovery is barred by reason of a showing that the representative of the injured shareholders was given, from time to time, such information that if he had caused it to be analyzed by counsel and accountants he might have been put upon inquiry sooner regarding the transactions in suit?

3. Whether, in such a suit, the Federal courts in Georgia were free to decide without reference to Georgia law that a financial agreement between husband and wife, residents of Georgia, by virtue of which the wife, who did not want a divorce, took such steps and proceedings that

she got one, is valid, and that the executory portion of such agreement is enforcible?

Statutes Involved

Pertinent provisions of the Georgia Codes of 1910 and 1933 are set out in the Appendix hereto, pp. 32-5, *infra*.

Summary Statement

Status of Parties: Joel Hurt, Sr. died in 1926, owning directly and through Atlanta Realty Corporation the controlling stock (2650 shares of common out of 3000 shares issued and outstanding) of Cotton States Fertilizer Company, a Georgia corporation. Other members of the Hurt family owned 300 shares more. Mr. Hurt's residuary estate, which included the controlling stock, was bequeathed in sixths to his widow, three sons and two daughters, "to be divided between them in kind, as far as may be practicable" (R. 224, v. I). The sons were Joel, Jr., who was one of the executors under the Will; Sherwood L., the petitioner herein; and George F., since deceased.

It is conceded that with respect to the transactions in suit Joel, Jr. acted for the executors of the estate and as the representative of his kin who owned the minority stock. In our further discussion we shall disregard Atlanta Realty Corporation's technical title, and treat the controlling shares as belonging to the decedent estate; also, we shall refer to the estate and the said minority stockholders collectively as "the vendors."

Respondent Clay had been with Cotton States since 1915 and its manager since 1920 (R. 107, v. I; R. 733, v. II). In 1926 he was also Secretary and Treasurer.

He enjoyed the trust and confidence of the decedent and his family. Shortly after Mr. Hurt's death he got the vendors to sell him their 2,950 shares on a down payment and a series of promissory notes secured by a pledge of the stock, none of the stock being deliverable until the purchase price had been paid in full. Respondent Howell was co-purchaser with Clay and financed the initial payment (R. 738, v. II), but he assumed no obligation to the vendors for the payment of the unpaid balance.

In 1927 Clay represented to the vendors that he could not meet the agreed instalments, and told them that he had gotten Thompson to come in on the purchase with him (R. 741, v. II; Defts. Ex. 65, R. 1343, v. II). The transaction was rearranged to provide for shares of the stock to be released from the pledge in proportion to the payments made and to be made; and new notes were given for the unpaid balance by Clay and Thompson, the latter acting through one of his companies, Niagara Sprayer Company (R. 743, v. II). Howell dropped out of the deal, except to the extent set out below.

Clay became a director of Cotton States in July, 1923, and President in May, 1926. He has held those offices and has been the active head of the business continuously since. Howell was Secretary and a director from May, 1926 to August, 1932. Thompson was an officer and director from November, 1927 to April, 1943, and Managing Director from September 28, 1940, to June 30, 1941.[3] He was a New York lawyer with an active practice, and in 1932 he delegated to the respondent O'Shaughnessey, as his confidential agent, an active part in the management of his interests in Cotton States and others of his enterprises. O'Shaughnessey became a director of Cotton States in August, 1932, and Treasurer in July, 1933, and

[3] Thompson was not found in the jurisdiction and is not a party to the suit.

has held those offices continuously since (R. 1949-50, v. III; R. 805-6, 925-8, v. II).

In 1932, as a result of the Howell transaction set out below, the vendors surrendered their unpaid notes and such common stock as still remained pledged to them, and accepted in exchange therefor 962 shares of Cotton States preferred, par value $100 per share, of which 884 1/5 shares went to the estate and the balance to the other vendors. In 1934, in connection with the Clay transaction set out below, the vendors wrote down their preferred stockholdings almost in half, the estate getting 495.1 shares and the other vendors 43.6. In 1943 the petitioner called upon his brother Joel, as sole surviving executor of their late father's estate, to bring a stockholder's derivative action to rectify the matters complained of herein, but, for lack of funds in the estate to finance such suit, Joel refused. Thereupon, on December 10, 1943, the petitioner bought the said 495.1 shares of preferred stock from the estate and the other 43.6 shares from the other holders.

No. 301 was filed June 14, 1944; dismissal for lack of status to sue was reversed in November, 1944, and rehearing was denied December 13, 1944. While the appeal in No. 301 was pending, and on August 17, 1944, the petitioner filed his complaint in No. 316. The history of No. 324 is as follows: On April 20, 1944 the petitioner made demand upon Cotton States to transfer the 495.1 shares of preferred into his name as record owner, but Cotton States refused. Four days later Joel, Jr. was removed as executor; on June 5 respondent Ellis was appointed administrator *de bonis non c.t.a.;* and on October 18 Ellis joined with respondent Mrs. Willie Martin Hurt in their complaint in the State Court in No. 324. The suit having been removed to the United States District Court, all three cases were tried as one and heard on appeal in the same way.

Howell Transaction [Question 1*a* of "Questions Presented"]: In 1932 Clay was financially embarrassed. Thompson was in a bad way too, so much so that he sent O'Shaughnessey to Georgia to try to raise money for him, with instructions that it did not matter what happened to Cotton States if only the desired money could be found (R. 925, 927, v. II). Clay considered having Cotton States issue to him bonds and preferred stock for use in satisfying his debt to the vendors, but was advised that he would have to pay value to the company for the bonds (Defts. Exs. 70, R. 1347, and 58, R. 1330, v. II). Instead, Clay and Thompson prevailed upon the vendors to agree to accept for their unpaid notes preferred stock of Cotton States to be thereafter lawfully authorized and issued (R. 758, 1111-12, v. II).

The position at this time was as follows: Clay, Thompson and Howell were the company's sole officers and directors. They owned 993⅓ shares each of Cotton States' outstanding 3,000 shares of common, par value $100 per share. A part of this stock was still pledged to secure the unpaid balance of $96,200 (in round figures) which Clay and Thompson owed the vendors. Howell and Planters Seed & Drug Company, a company in which Howell was interested, owed Cotton States $49,051.58.

Clay, Thompson and Howell thereupon did the following:

At a stockholders' meeting held July 19, 1932 (Pltfs. Ex. 15, R. 1109-14, v. II) amendments to the charter were voted, to authorize (a) issuance of $100,000 par value preferred, (b) conversion of 1,000 shares of common, share for share, into preferred, and (c) acceptance by the corporation of its stock in payment of debts owing to it. Also, a resolution was adopted that "the corporation accept from S. F. Howell, 494 shares of common stock now standing in his name and owned by him, and 333⅓ shares of preferred stock as soon as it shall have been converted from common to preferred, in full payment of his indebt-

edness and that of Planters Seed & Drug Company to this company, amounting to the sum set forth in contract with him of this date." However, the contract with Howell "of this date" does not appear in the minutes. It released Howell and Planters Company in consideration of Howell's agreement to transfer to Cotton States 827⅓ shares of its common owned by him, or, at the option of Cotton States, such of the said common shares as would remain after conversion of 333⅓ of them by Howell into preferred stock (R. 42, v. I). Thereafter, the Cotton States charter having been amended as set forth above, Cotton States accommodatingly "elected" to receive from Howell in payment of his and Planters Company's debts, instead of the 827⅓ shares of common, only such shares of common as remained after Howell had converted 333⅓ shares into a like number of shares of the newly authorized preferred (Pltfs. Ex. D-3, R. 259, v. I; Defts. Ex. 180, R. 1533, v. III).[4] These 333⅓ shares of preferred were issued to Howell, and he then divided them, 320⅔ going to Clay and Thompson, who paid Cotton States nothing for them, and the remaining 12⅔ to Cotton States. Clay and Thompson each added to these 320⅔ shares an equal number of shares of preferred which they had respectively procured by conversions of the necessary shares of their own common, and transferred the total of 962 preferred shares which they had thus put together to the vendors, in payment of their $96,200 debt (stub of Pltfs. Ex. D-4, R. 261, v. I, showing the source of the 884 1/5 shares that went to the estate; also Defts. Ex. 179, R. 1532, v. III).

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[4] Defts. Ex. 180 is Cotton States' receipt to Howell for 547⅓ shares of common in full settlement of his and Planters Company's debts. We have not been able to find in the record any explanation for the difference of 53⅓ shares between the 494 mentioned in the minutes of the stockholders' meeting, R. 1109-14, and the 547⅓ receipted for.

Through this device Howell and his company got released; Clay and Thompson paid off the vendors in substantial part with property of Cotton States which had cost them nothing, and got their shares of common released from the pledge; and Clay and Thompson ended up owning practically all the common stock of Cotton States instead of only two-thirds.

Clay Transaction [Question 1*b* under "Questions Presented"]: In 1933 Clay had overdrawn his account with the company to the extent of $17,509.11. At a meeting of the board held July 22, 1933 (Pltfs. Ex. 15, R. 1125, v. II), Clay being present and voting, the treasurer was authorized to accept from Clay 338 shares of the company's common stock in full settlement of the debt. A year later this had not yet been carried out, and Clay's debt had risen to $18,352.75. At a meeting of the board held July 21, 1934 (Pltfs. Ex. 15, R. 1136, v. II), Clay being again present and voting, the increased indebtedness was directed to be satisfied for the same consideration; and this time the transaction was carried out. Cotton States was admittedly bankrupt (R. 1013, v. II), and the stock was worthless. Clay's explanation for the delay (R. 817, v. II) was a plain admission that during this interval he was, in effect, "playing the market" against his company.[5]

In justification it was testified that in 1934 Cotton States was applying for an RFC loan, and that the Atlanta agency manager of the RFC advised the company "to charge off anything that was worthless and make the application based wholly on sound assets" (R. 1013, v. II). However, the possibility of applying for such a loan

[5] The following was his explanation: "Well, I guess I was too optimistic. I was thinking all the time maybe this depression would stop and things would turn out better, and I really thought there was a chance of conditions improving and I really preferred to hold the stock and try to work the thing out, but they didn't. There was no change in conditions. So, when we began to clean out in June of 1934, I thought the best thing to do was to go ahead and charge it off."

was not considered until May, 1934 (R. 932, v. II; Pltfs. Ex. 7, R. 33, v. I). Furthermore, what the RFC was after could have been perfectly well, and properly, accomplished by setting up against Clay's indebtedness a reserve which would value it down on the books to whatever figure the board might consider reasonable, and in due time Clay could have paid off what he owed—if he was interested in dealing fairly with the company. Certainly the RFC was not conditioning its loan to Cotton States on the company making a gift of this debt to its president and director.

Thompson Transaction [Question 1*c* under "Questions Presented"]: In 1942-3 Cotton States was showing substantial profits and its prospects were good. The directors decided that the company should try to buy up certain obligations of long standing (R. 938-49, 990-1, v. II). They included trade debts; notes owing to Thompson, amounting (with interest to April 30, 1943) to $18,866.55; and an unpaid item of $2,500 salary to Thompson. As at April 30, 1943, these purchases had been accomplished. Clay and O'Shaughnessey bought up the claims personally, but did so, on their own testimony, in the company's behalf. Their purchase from Thompson comprised, in a single transaction, acquisition of his notes, his salary claim, and his Cotton States stock (7.1 shares preferred and 607⅔ shares common). At the trial Clay and O'Shaughnessey claimed that they paid Thompson $27,500 for the above.

Clay and O'Shaughnessey then proceeded, however, to treat their purchases as though they had been made for personal account. Certain selected obligations acquired by them they set up on the company's books as obligations owing to themselves—not in the amount which they claimed to have paid for them, which was $25,474.86, but in their full amount, both principal and interest, as at April 30, 1943, *viz.*, $55,934.82 (Pltfs. Ex. 1, R. 1026, v. II, item: "Notes Payable: For Money Borrowed from Indi-

viduals * * * $55,934.82"; and see Pltfs. Ex. 15, R. 1187, v. II). That left unaccounted for Thompson's $2,500 salary claim, and his stock. The salary claim was washed out as described at R. 947-8, v. II, by having Cotton States pay it back to Clay and O'Shaughnessey at once. The stock Clay and O'Shaughnessey simply took over, each taking half the common (R. 1039, v. II). The above set-up, recorded in completely blind entries on the books as at June 30, 1943, was continued on the books as at June 30, 1944 (Pltfs. Ex. 2, R. 1067-8, v. II).

But the Circuit Court of Appeals having sustained petitioner's status to sue in November, 1944, and rehearing having been denied December 13, 1944, Clay and O'Shaughnessey created the minutes of December 30, 1944 (Pltfs. Ex. 15, R. 1183-92, v. II). These purport to explain and justify the blind entries in the 1943 and 1944 accounts regarding "money borrowed from individuals." To that end the minutes set out an accounting which indicated that Clay and O'Shaughnessey had bought for $25,474.86 obligations of the company totaling as at April 30, 1943 the above sum of $55,934.82. The minutes then go on to provide that Cotton States shall buy back these obligations from Clay and O'Shaughnessey at the April 30, 1943 cost to them of $25,474.86 plus interest to December 30, 1944, aggregating the sum of $28,022.35, Clay and O'Shaughnessey on their part agreeing to lend back $28,000 to the company at 5%. Once again, the shares of stock acquired from Thompson are omitted from the accounting.

The claim now made by Clay and O'Shaughnessey that they paid Thompson $27,500 for his notes, accounts, and shares of stock is not true. Under date June 9, 1943 Clay wrote Joel Hurt (Pltfs. Ex. 13, R. 53, v. I): "Mr. Thompson sold his common stock, along with his notes and accounts which the Company owed him, for a lump sum which amounted to less than the face value of the notes and accounts plus accrued interest. It was for this

reason that I said in my previous letter that he received very little, if anything, for his common stock." Clay stood on the truth of this statement at the trial (R. 383, v. I). But Thompson's notes and accounts, plus interest, amounted to only $21,366.55 ($18,866.55 at R. 1187, where the items are wrongly totaled at $18,852.33, plus the $2,500 salary claim). Clay and O'Shaughnessey thus got Thompson's stock for practically nothing, as appears from the following, where we have set up the transaction using both the amounts which respondents now claim they paid, and the figures confessed in Clay's June 9 letter:

From Whom Purchased (R. 1187 plus testimony at R. 938-49 and 990-1)	*Total Purchased*	*Am'ts. Claimed to Have Been Paid*	*Am'ts. Actually Paid* (per trial testimony and June 9 letter re Thompson deal)	
Am. Cyanamid	$22,228.76	$100.00	$100.00	
Niagara Sprayer	9,050.00	1,250.00	1,250.00	
Baker	516.98	1.00	1.00	
Thompson	18,866.55[6]	25,000.00 } [8]		
	2,500.00[7]	2,500.00 }	21,366.55	minus[9]
Clay	4,901.00	4,901.00	4,901.00	
O'Shaughnessey	371.53	371.53	371.53	
Totals:	$58,434.82	$34,123.53	$27,990.08	
Less am't repaid to Clay and O'S		27,974.86[10]	27,974.86[10]	
Cost of Thompson stock to Clay and O'S		$6,148.67	$15.22	

[6] Reflected at R. 1187, v. II.

[7] Not reflected at R. 1187.

[8] Total of $27,500 which Clay and O'Shaughnessey now claim they paid Thompson.

[9] See quotation from Clay's June 9 letter, *supra*.

[10] $2,500 paid back by Cotton States to Clay and O'Shaughnessey at the time of the purchase from Thompson (R. 948, v. II), plus $25,474.86 thereafter repaid to them (R. 1189, v. II).

Disregarding the preferred shares, Clay and O'Shaughnessey thus made a secret purchase, at the price of 2½ cents per share, of more than 60% of all the outstanding Cotton States common. The company had at June 30, 1943, total assets of $300,946.69, and net worth of $172,636.55. In the very year in which the purchase was made the company's net profit was $44,550.75 (Pltfs. Ex. 1, R. 1016-7, v. II); and in point of fact the company was worth substantially more than is set out above, because liabilities were inflated by improper salary accumulations for officers as set out in the next part of our discussion. These very accumulations furnished, in large part, the money with which Clay and O'Shaughnessey bought out Thompson (R. 1022, v. II; R. 949, v. II).

Salaries and Bonuses [Question 1*d* under "Questions Presented"]: At a meeting of the directors held August 2, 1932 (Pltfs. Ex. 15, R. 1116, v. II), Clay's salary was reduced from $6,000 per year to $3,000, by reason of the company's straitened condition. At a meeting of the board held January 2, 1934 (Pltfs. Ex. 15, R. 1127, v. II) O'Shaughnessey was voted compensation at the rate of $2,600 per year.

In 1934, upon the precise ground that the company was in bad shape and that all parties in interest must make sacrifices (R. 33, v. I), Clay, Thompson and O'Shaughnessey prevailed upon the vendors (now preferred stockholders) to write down their stock by substantially one-half (Pltfs. Ex. 15, R. 1149-51, v. II). "I am confident," Clay wrote Joel Hurt, that an appropriate rearrangement of the stock "would enable us to obtain a RFC loan" (R. 34, v. I). However, hardly had the RFC loan been closed when Clay's salary was restored retroactively to the $6,000 figure, and O'Shaughnessey's raised retroactively to $4,800 (cf. Pltfs. Ex. 15, R. 1135, v. II, with same exhibit R. 1139). At the meeting at

which this was done Clay and O'Shaughnessey were present and voted for this action.

At this time Cotton States was losing money at such a rate that these increased salaries could not be actually paid. During the years 1933 to 1941, when the net losses totaled $112,405, credits totaling $17,800 were accumulated on the company's books in favor of Clay and O'Shaughnessey (Defts. Ex. 195, R. 1865, v. III). Clay took the precaution to ascertain from counsel that these accruals, being debts, would come ahead of dividends on the preferred stock (Defts. Ex. 25, R. 1239-40, v. II).

In 1942 Cotton States began making money. Immediately bonuses were voted to Clay and O'Shaughnessey. On June 26, 1942, bonuses of 40% ($2,400 to Clay, $1,920 to O'Shaughnessey) were voted retroactively for the fiscal year ending June 30, 1942 (Pltfs. Ex. 15, R. 1177, v. II). On September 4, 1942, like bonuses were voted for the fiscal year ending June 30, 1943 (Pltfs. Ex. 15, R. 1179, v. II). On June 30, 1943, retroactive additional bonuses of 25% were voted for each of the fiscal years ending June 30, 1942 and June 30, 1943 (Pltfs. Ex. 15, R. 1182, v. II). On December 30, 1944 the board "ratified" bonuses of 65% which had been paid without any record of corporate action during the fiscal year ended June 30, 1944 (Pltfs. Ex. 15, R. 1183-4, v. II). In addition, it was testified that similar bonuses have been voted for the fiscal year ending June 30, 1945 (R. 891, v. II). In the aggregate, Clay and O'Shaughnessey voted themselves during the years 1942-5, practically all retroactively, bonuses of $19,500 and $15,600, respectively, or a total of $35,100.

Knowledge and Acquiescence [Question 2 under "Questions Presented"]: It is not feasible to discuss herein, in detail, the respondents' testimony upon which the courts below based their holdings in this regard. However,

analysis of the record shows that it is possible to classify this testimony into two general categories:

1. From time to time there were sent to Joel Hurt, Jr., as representative of the vendors, and/or to the petitioner herein, copies of balance sheets, statements of assets and liabilities, and profit and loss statements. The respondents introduced a mass of them in evidence, comprising 22 exhibits and occupying over 450 pages of the Record. These data were sent irregularly, and were generally furnished two to three years late (R. 445-6, v. I). On one occasion the vendors had to retain counsel in order to get the data, and, after a number of months' delay, they were compelled to accept a niggardly compromise under which their representative was allowed to look at the reports in counsel's office but forbidden to copy anything from them (Defts. Exs. 12-23, R. 1227-37, v. II). Close scrutiny of these data, and comparison of earlier with later reports, would have disclosed changes in certain of the accounts, but would have told nothing about the true character of the transactions which they reflected. To arrive at the latter, it would have been essential to get at records which were not made available to the vendors until September, 1943, and some of which they did not see until the trial (R. 501-5, 510, v. I). For example, nobody representing the vendors saw the Cotton States minutes before September, 1943. Even if they had been allowed to see the minutes of the July 19, 1932 meeting at which the Howell transaction was approved (R. 1109-14, v. II), they would only have been misled, since the contract of the same date (R. 42, v. I) was not in the minutes, and only careful comparison of those two, followed up by examination of the books to see what was actually done, would reveal the impropriety of this deal. The Thompson deal, as has been shown, was unrecognizable in the accounts and was affirmatively misstated in the corporate minutes. The vendors would have needed, not

diligence alone, but clairvoyance, to get at the truth of the transactions in suit from these data.

2. The respondents testified under careful leading, with sweeping inclusiveness, that in connection with the transactions in suit the representatives of the vendors were told everything that was done, when it was done. Where the respondents were testifying about alleged word-of-mouth disclosures, their testimony was general and conclusory, not factual; and where it was tested out it did not stand up. One instance must suffice. Thompson testified with respect to the Clay transaction that Joel Hurt, Jr. "was kept informed of this whole transaction that was involved * * * he was kept advised thoroughly all the way through" (R. 704, v. I); but on cross-examination he could not even remember that Clay's indebtedness had been satisfied, let alone how. All he could say was (R. 722, v. I): "I do not remember the circumstances or the details, but something was done by him at that time to lower his indebtedness." The respondents' writings stand scrutiny no better. Here again we confine ourselves to one example. Clay's June 9 letter to Hurt told the truth about the price which had been paid to Thompson, but this was followed immediately by the vitally important falsehood that neither Clay nor O'Shaughnessey had any interest in the purchase. This is readily established by comparing the pertinent language in Clay's letter, R. 53-4,[11] with the facts as disclosed during the trial (R. 938 *et seq.* and R. 1184 *et seq.*, v. II).

[11] It reads: "His [Thompson's] stock, notes and accounts were purchased in the name of the writer and W. J. O'Shaughnessey but a third party furnished the money and has a claim on all of Thompson's former holdings in the Company, as well as on mine and Mr. O'Shaughnessey's. * * * It is this third party, whose identity I cannot disclose, who would have to put up the money for the purchase of the preferred stock if an agreement can be had with the present owners as to its value."

Validity of Guaranty Agreement [Question 3 under "Questions Presented"]: The late George F. Hurt and Mrs. Willie Martin Hurt were husband and wife. The husband was anxious to get a divorce, but his wife did not want one (R. 2262, v. V). The husband filed suit nevertheless in December 1921, alleging cruelty (R. 2517-19). His wife cross-complained for divorce within a few days upon allegations which greatly scandalized the family (R. 2520-22), and then particularized her allegations so as to make them even more hurtful (R. 2524-6). The parties were at a bitter impasse, and the husband's suit and the wife's cross-suit idled on the docket of the court for almost a year.

In October, 1922 the parties entered into an agreement under which the husband undertook to pay substantial alimony (Defts. Ex. 178, R. 1523-9, v. III). The effectiveness of the agreement was conditioned upon the payments being guaranteed by the husband's father (par. 7 at R. 1527), which was not done until November (R. 1529). Additionally the agreement recited in paragraph 6 that "Mrs. Hurt is seeking a divorce from Mr. Hurt on the ground of desertion." That was not true. The wife's cross-complaint did not mention desertion. The quoted statement was an inadvertent admission of what the parties were really agreeing to do, and, in fact, did shortly thereafter. On January 8, 1923 the wife amended her cross-complaint so as to add an allegation of desertion. The husband then struck all the material allegations of his complaint, in effect withdrawing his action (R. 2526). Thereupon, on January 19 the wife further amended her complaint by striking the scandalous matter (R. 2527), and within a few days (February 6, 1923) the case was tried as an undefended suit by the wife against the husband, and she got her verdict on the ground of desertion (R. 2516).

Specification of Errors to be Urged

The Circuit Court of Appeals erred as follows:

(1) In Nos. 301 and 316:

(A) In holding without reference to Georgia law, and contrary thereto, that none of the transactions hereinabove set out "were illegal, done in fraud of the company, or otherwise exceptionable."

(B) In holding without reference to Georgia law, and contrary thereto, that ambiguous and equivocal disclosures to the injured shareholders barred recovery in the company's behalf for the said transactions.

(2) In No. 316:

(A) In holding that the petitioner had abandoned his appeal therein.

(B) In affirming dismissal on the ground that the stock, in right of which petitioner sues, was acquired by him after the occurrence of the things he complains of.

(3) In No. 324, in holding without reference to Georgia law, and contrary thereto, that the guaranty agreement is an enforcible obligation, and that the respondent Willie Martin Hurt is a creditor of the estate of Joel Hurt, Sr. by virtue thereof.

REASONS RELIED ON FOR GRANTING THE WRIT

I

In Nos. 301 and 316 the Court below has decided important questions of local law regarding the fiduciary responsibility of corporate officers and directors without reference to local law and in a way which is in conflict therewith.

A

"The source of substantive rights enforced by a Federal court under diversity jurisdiction, it cannot be said too often, is the law of the States" (*Guaranty Trust Co.* v. *York*, 326 U. S. 99, 112). In the cases at bar this mandate has been ignored. The courts below have proceeded without reference to controlling Georgia law, and plainly contrary thereto.

Standing on their own bottoms, the Howell, Clay and Thompson deals are classically simple instances of corporate officers and directors misappropriating company property and dealing with their company to their own enrichment. This conduct has been justified below, without any citation of authority whatever, on the ground that in consideration of their unlawful gains the officers and directors concerned made great exertions at a time when the company needed their utmost efforts, and that all things considered, the preferred stockholders may win back in the future, from the hoped-for success of these exertions, more than they have lost up to now by the misconduct. Upon this rationalization the Circuit Court of Appeals, adopting the respondents' argument, concluded that there was no accountability. The nub of the opinion below on this aspect of the case is in the following sentence (159 F. 2d at p. 57; R. 2595, v. V):

> "The fact that the company is now in greatly better shape than it was in then, that it has been yearly getting in better shape, that the R. F. C. loan

is about to be, or has already been, paid off, and that in time, the preferred stock, if conditions continue as at present, will be on a dividend basis and have real value, testify not only to the absence of fraud doing but to the wisdom and general fairness of the course then pursued and completely explain, indeed justify, acts now seized upon by plaintiffs as fraudulent outrages."

This sets up the intolerable principle that a trustee may have unlawful profits from the estate as incentive pay for exerting himself on its behalf. Two corollaries to this proposition, which the Court below also accepted, are that the trustee's accountability is conditioned upon and measured by the *cestui's* loss instead of the trustee's forbidden gains, and that when the *cestui* comes into equity for relief, he has the burden of showing damage and proximate cause; quite as though the action was for negligently operating a vehicle.

This is contrary to Georgia case and statute law. "All the authorities agree that he [the director] is a trustee for the company."[12] The respondents conceded below that this is Georgia law (R. 860, v. II; Defts. Ex. 58, R. 1331, v. II). However, they were allowed to escape the consequences through arguments in avoidance which Georgia law refuses to tolerate. " 'The trustee shall not use the trust funds to his own profit. He shall be liable to account for all such profits made.' Code of 1910, §3767; Code of 1933, §108-429. This principle applies where a fiduciary relation exists between the parties, whether or not the person occupying the position of trust is a technical trustee."[13] The Georgia rule is that

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[12] *Oliver* v. *Oliver*, 118 Ga. 362, 367. Even when the director is bargaining privately with an individual stockholder, "no amount of argument can destroy the fact that the director is, in a most important and legitimate sense, trustee for the stockholder" (*ibid*; cited with approval in *Strong* v. *Repide*, 213 U. S. 419, 431).

[13] *Swann* v. *Wright*, 180 Ga. 323, 326-7. See also Code §§22-711 and 37-708, pp. 32, 34, *infra*.

the fiduciary "can make no profit for himself out of the trust estate. If he risk the trust funds and lose, he is compelled to account for their full value; if he is successful, he is required to pay what he gains to the beneficiary of the fund embarked in the enterprise. This rule applies not only to trustees eo nomine, but to all persons sustaining confidential relations to others, such as executors and administrators, guardians, agents, officers, partners, etc."[14] It was further held in this case[15] that the fiduciary is forbidden to traffic in the estate "whether he acted bona fide or not, or whether actual gain resulted to him or not."

The offending fiduciary argued good faith and fairness in *Haley* v. *Atlantic National Fire Ins. Co.*, 151 Ga. 158, 163; but the Court said:

> "We do not assert that Mrs. Haley acted in bad faith. Under the authorities, the question of good faith, in such circumstances, is immaterial. It may be that the purchase by Mrs. Haley was in fact advantageous to the estate. This argument has been often advanced, and as often rejected. The broad rule of equity, applicable alike to agents, partners, guardians, executors, administrators, and directors and managing officers of corporations, is that it is the duty of a trustee not to accept any position or to enter into any relation or to do any act inconsistent with the interest of the beneficiary."[16]

The Georgia courts have adhered to the above principles with unbroken uniformity.[17] In so doing they not only obey the statutory mandate,[18] but are also in accord with—and have, indeed, expressly followed—the great

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[14] *Fricker* v. *Americus Improvement Co.*, 124 Ga. 165, 175.

[15] *Ibid*, p. 176.

[16] Citing Pomeroy, and Federal and New York cases.

[17] *Caldwell* v. *Hill* (1934) 179 Ga. 417, 425; *Perdue* v. *McKenzie* (1942) 194 Ga. 356, 364-5.

[18] Code §§22-711, 37-708, and 108-429, pp. 32-3, 34, and 35, *infra*.

Federal landmarks. The *Fricker* case, *supra*,[19] cites and follows *Wardell* v. *Union Pacific R. R. Co.*, 103 U. S. 651, 658, where it was held that corporate officers and directors are absolutely forbidden to put themselves in a position of "conflict between interest and duty" with respect to anything affecting the subject-matter of their trust, and that they cannot "enter into nor authorize contracts on behalf of those for whom they are appointed to act, and then personally participate in the benefits." In the *Haley* case, *supra* (151 Ga. at 163) the Court approves *Trice* v. *Comstock*, 121 Fed. 620, 623, where Sanborn, J., wrote that the "inexorable principle" of a trustee's unconditional accountability for the profits of self-dealing "is not based upon, or conditioned by, the * * * injury or damage which the betrayal of the confidence given entails. It rests upon a broader foundation, upon that sagacious public policy which, for the purpose of removing all temptation, removes all possibility that a trustee may derive profit from the subject-matter of his trust, so that one whose confidence has been betrayed may enforce the trust which arises under this rule of law although he has sustained no damage."[20]

With respect to the salary increases and bonuses the courts below proceeded similarly without reference to Georgia law. The Circuit Court of Appeals recognized that Clay and O'Shaughnessey "did not have the power to vote themselves back salaries * * * and will be prevented from exercising that power when, as here, it is apparent that the result, if not the purpose, of the voting,

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[19] *Fricker* v. *Americus Improvement Co.*, 124 Ga. at p. 176.

[20] The Clay transaction was tainted with the further impropriety that it was a purchase by an insolvent company of its own stock. In *Fitzpatrick* v. *McGregor*, 133 Ga. 332, 342, the Court said: "We know of no case wherein it is held that an insolvent corporation has the power to purchase its own shares of stock." *Cf.* Code §22-709, p. 32, *infra*.

is to impose on the preferred stockholders."[21] That was sound enough as far as it went, since in Georgia corporate officers are forbidden retroactive awards of compensation precisely because they are trustees, wherefore they come under the rule that the law does not imply any promise to pay trustees for performing their duties as such.[22] However, in reaching the result that these respondents are accountable only for impositions retroactively perpetrated, and not for impositions currently perpetrated, the Court missed the whole point—to-wit, that imposition on the stockholders is the basic vice, which is aggravated by retroactivity, but does not depend therefrom.[23] On this score the courts below had before them, but wholly disregarded, the specific statutory provisions that the fiduciary "shall not use the trust funds to his own profit," and that, in consequence, corporate officers and directors are forbidden from "acting in their own interest in a manner destructive of the company, or of the rights of the other stockholders," and are further forbidden from "oppressively and illegally pursuing in the name of the corporation, a course in violation of the rights of the stockholders."[24] Under these statutory mandates together with the further Georgia authority already cited by us, the courts below had ample guidance to show them, without more,[25] that under Georgia law directors are forbidden to vote themselves as officers such salaries as practically amount to a division among themselves of the earnings

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[21] 159 F. 2d at p. 59 (R. 2598, v. V).

[22] *Home Mixture Guano Co.* v. *Tillman,* 125 Ga. 172, 179-80.

[23] As a matter of fact the Circuit Court of Appeals was not consistent even in this regard, condemning some but refusing to condemn others of the retroactive payments.

[24] *Swann* v. *Wright, supra,* 180 Ga. 323, 326-7; Georgia Code §§108-429 and 22-711, pp. 35 and 32-3, *infra;* and cf. Code §37-708, p. 34, *infra.*

[25] Cf. *Meredith* v. *Winter Haven,* 320 U. S. 228, 237.

of the corporation; that good faith requires them to adapt their compensation fairly to the financial condition of their company; and that when the company is suffering operating losses and inroads on its capital, it is bad faith on its face for the officers and directors to accumulate claims against it, as was done here, with the purpose of coming ahead of stockholders if and when the company's fortunes take a turn for the better. Particularly is this true when the salary increases and bonuses are awarded to themselves by directors who have voted themselves in as directors by means of their own stock control, and then, as directors, vote themselves into office and grant themselves the excessive compensation.[26]

B

Equally did the courts below proceed without reference to Georgia law, in holding that the respondents' unfrank "disclosures" sufficed to charge the injured stockholders with knowledge of the acts complained of. Suppression of a material fact is itself fraud where there is a duty to be frank, as, for example, between parties in

[26] The Court could also have looked, if it had wished, to such cases as *Backus* v. *Finkelstein,* 23 F. 2d 531, 537 (approved by the Fifth C. C. A. in *Flint River Pecan Co.* v. *Fry,* 29 F. 2d 457, 459), and *Decatur Mineral Land Co.* v. *Palm,* 113 Ala. 531, since they proceed on basic premises identical with those which prevail in Georgia. In the *Decatur* case the Court said (113 Ala. at 537): "These salaries not only consumed all the income, but encroached annually upon the capital assets, and if continued, would eventually leave nothing for the stockholders. The duty of a director is to act for the interest of the stockholders, and manage the affairs of the corporation for their benefit, and not for his personal gain. There was a direct conflict between the duty owed by these directors to the stockholders, and their self interest; and, as is frequently the case under such conditions, the frailty of human nature sacrifices duty to self interest. They fixed the salaries at exorbitant prices, then elected themselves to the offices. The fact that the president may have been unwilling to accept the office at a less salary, proves nothing in favor of the fairness and reasonableness of the amount."

confidential relations.[27] Under Georgia law it is not enough for a person in a fiduciary capacity to say, as Sir George Jessel put it,[28] "I gave you sufficient information to put you upon inquiry." This applies with full force to corporate officers and directors, because "the peculiar powers and special opportunities of these fiduciaries call for an enlargement rather than a restriction of the rule requiring disclosures," and the obligations of office of a company director "bring him peculiarly within the general doctrine which declares that concealment of material facts may of itself amount to a fraud."[29] Georgia law on this point is thus in line with what was written by the late Chief Justice in *Rogers* v. *Guaranty Trust Company,* 288 U. S. 123, 141:[30]

> "They [the stockholders] were entitled to read the proposal in the light of the fundamental duty of directors to derive no profit from their own official action, without the consent of the stockholders, obtained after full and fair revelation of every circumstance which might reasonably influence them to withhold their consent. [Citing cases.] They were entitled to assume that the proposal involved nothing which did not fairly appear on its face and above all that it was not a cloak for a scheme by which the directors were to enrich themselves in great amounts at the expense of the corporation, of whose interests they were the legal guardians."

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[27] Georgia Code, §§37-704, and 96-203, pp. 33-4 and 34-5, *infra; Little* v. *Haas,* (D. C., N. Dist. Ga. 1946), 68 Fed. Supp. 545, 555.

[28] *Dunne* v. *English,* L. R. 18 Eq. 535.

[29] *Oliver* v. *Oliver, supra,* 118 Ga. at 371.

[30] This case did not involve Georgia law, but no difference is perceived between the above and the Georgia rule. While the late Chief Justice's was a dissenting opinion, there was no division among the Court regarding the rule of required disclosure.

C

Not one Georgia case or provision of statute was cited by the District or Circuit Court of Appeals to support their holdings; and all the pertinent decisions and Code provisions that we have found condemn them.[31] The lower courts completely ignored substantive local law in their disposition of these cases, in violation of this Court's mandates regarding the only right basis for decision in diversity jurisdiction cases. The holdings at bar have introduced into the substantive law of Georgia concerning the obligations of corporate fiduciaries that "double system of conflicting laws in the same State," which this Court has called "plainly hostile to the reign of law" (*Guaranty Trust Co.* v. *York, supra,* 326 U. S. 99, 112). Such action calls for an exercise of this Court's power of supervision.

II

In No. 316 the Court below proceeded in plain disregard of the record.

In No. 316, as in the other two cases, the petitioner gave timely notice of appeal to the Circuit Court of Appeals, and filed his appeal bond seasonably (R. 2056-8, v. IV). The Circuit Court of Appeals noted in its opinion herein that the three cases, though not consolidated, were tried and submitted on appeal together (159 F. 2d at p. 54; R. 2588, v. V). The substantive issues were the same in No. 316 as in No. 301, and, naturally enough, counsel argued them together on the appeal. There was no jus-

[31] Indeed, the only Georgia case cited at all on these aspects was *Mathews* v. *Fort Valley Cotton Mills,* 179 Ga. 580, in footnotes 6 and 7, 159 F. 2d, pp. 58-9 (R. 2597-8, v. V), but in the text the Court itself recognized the inapplicability of this decision to the preferred stockholders in the actions at bar.

tification, therefore, for the holding that "appellant has abandoned here his appeal from the judgment in cause No. 316."

Nor was there any justification for the holding "that the stock, in right of which plaintiff sues, was acquired by him after the occurrence of the things he complains of" (159 F. 2d at p. 60; R. 2600, v. V). Petitioner acquired this stock December 10, 1943, whereas the Court recognized that there was ground for complaint "in respect of bonuses and additional compensation voted for 1944 and 1945," and remanded in No. 301 for proof as to them (159 F. 2d at pp. 60-1; R. 2601-2, v. V).

III

In No. 324 the Court has decided important questions of local law regarding validity of contract without reference to local law and in a way which is in conflict therewith.

In this action there are three controlling facts, two of which are not open to dispute, and the other of which is an inference compellingly required by the first two. These are: *first,* that the wife, Mrs. Willie Martin Hurt, did not want a divorce; *second,* that she and her husband were at an impasse which threatened to make it impossible for him to get divorced; and *third,* that to end the stalemate a financial agreement was entered into between husband and wife for the purpose, and with the effect, of inducing the wife to carry through the necessary proceedings to obtain a divorce.

In form, the agreement does not spell out in so many words that the wife's cooperation was being bought. In substance, that is exactly what the agreement provides. In fact, that is exactly what the agreement accomplished.

Under Georgia law such an agreement—"any agreement conditioned on the obtainment of a divorce, or in-

tended or calculated to facilitate its obtainment''—is void *ab initio* as against public policy.[32]

An agreement thus tainted cannot be made good by subsequent partial performance; nor can it be sustained upon any plea of ratification or estoppel. The public policy which makes the agreement void would be of no force if the parties could make the agreement binding by their own acts done under it.[33]

The fact that respondent Ellis, as administrator, contended below for the validity of this agreement is immaterial. Where an agreement offends public policy the administrator or executor can no more make it good by partial performance, estoppel, or concession of validity, than could his deceased (21 Am. Jur. 501, §230). We do not go into the question whether Mr. Ellis was in the proper discharge of his duty as administrator in making no effort in No. 301 to support the claims put forward by the petitioner in behalf of Cotton States, though one of those claims was held good on appeal and others of them may be held good on the remand, and in litigating in No. 324 in support of, rather than opposition to, a contested claim against his estate (21 Am. Jur. 575, §339). This much is clear, that the respondents take nothing by Mr. Ellis' position in these regards, either in No. 301 or in No. 324.

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[32] *Birch* v. *Anthony*, 109 Ga. 349; *Heath* v. *Philpot*, 39 Ga. App. 108; *Craig* v. *Craig*, 53 Ga. App. 632; *Ozmore* v. *Ozmore*, 179 Ga. 339; *Law* v. *Law*, 186 Ga. 113.

[33] Georgia Code, §§20-501 and 20-504, p. 32, *infra*. In *Bryson* v. *Keith*, 186 Ga. 616, 618, it was held: "If the contract [founded upon an illegal or immoral consideration] is executed, it will be left to stand; if it is executory, neither party can enforce it."

IV

The "two-court rule" does not preclude review herein.

The District Court's Findings regarding the Howell transaction go at length into the reasons why Cotton States settled with Howell and Planters Company for Howell's stock, but they are silent as to the diversion of almost 40% of the consideration (320⅔ shares out of 827⅓) to Clay and Thompson (Findings 21, 24, 25, 26, R. 1937-9, and Finding 63, R. 1950-1, v. III). The Findings regarding the Clay transaction mention, but give no effect to, Clay's "heads I win tails you lose" treatment of Cotton States from July, 1933 to July, 1934, and adopt as justification the irrelevant—and distorted—alleged recommendation of the RFC (Findings 27, 28, and 64, R. 1939-40 and R. 1951, v. III). The Findings regarding the Thompson transaction wholly ignore, as did the respondents in their pre-trial disclosures, the crux of that deal, *viz.,* the stock transaction (Findings 67-9, incl., R. 1951-2, v. III). The facts ignored are the very essence of the improprieties; yet the vendors have been charged with knowledge of what the Court itself missed or ignored; and the facts which were found, taken together with the results arrived at, show acceptance by the District Court of excuses that are inadmissible under controlling local law. The conclusory "Findings" (No. 57 as to salaries, No. 70 as to everything in suit—R. 1949 and 1952, v. III) are not true findings of fact, but "the ultimate judgment"[34]—and the facts proved and found do not support them. The Circuit Court of Appeals accepted the untenable excuses and approved the conclusory "Findings." The holdings below are not supported by concurrent findings of fact. They are vitiated, rather, by concurrent mis-

[34] *Baumgartner* v. *U. S.,* 322 U. S. 665, 670.

apprehension of law as to the right basis for decision in diversity jurisdiction cases.

So much for No. 301, with which is coupled No. 316. As to No. 324, only questions of law are presented, and these were decided contrary to local law.

How little these cases turn on disputed issues of fact will be clear, we think, from the face of this petition, wherein, out of 89 citations to the record, 63 are citations of undisputed documents, 24 are citations to the respondents' own testimony, and only 2 are citations to petitioner's testimony.

Under the holding in *Baumgartner* v. *U. S.*, 322 U. S. 665, the two-court rule does not preclude review herein.

WHEREFORE, it is respectfully submitted that the writ of certiorari herein prayed should issue.

April, 1947.

S. L. HURT,
Petitioner.

MURRAY C. BERNAYS,
Counsel for Petitioner.

JOHN L. WESTMORELAND,
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Of Counsel.

APPENDIX

Georgia Code of 1933, effective January 1, 1935 (numbers in parentheses are the corresponding sections of the 1910 Code)

§20-501 (4251) **Contracts to do immoral or illegal thing.**—A contract to do an immoral or illegal thing is void. If the contract be severable, that which is legal will not be annulled by that which is illegal.

§20-504 (4253) **Contracts against public policy; illustrations.**—A contract which is against the policy of the law cannot be enforced; such are contracts tending to corrupt legislation or the judiciary, contracts in general restraint of trade, contracts to evade or oppose the revenue laws of another country, wagering contracts, contracts of maintenance or champerty.

§22-709 (2222) **Directors of insolvent corporations; duties.**—Directors primarily represent the corporation and its stockholders, but when the corporation becomes insolvent they are bound to manage the remaining assets for the benefit of its creditors, and cannot in any manner use their powers for the purpose of obtaining a preference or advantage to themselves.

§22-710 (2223) **Majority of stockholders entitled to control.**—So long as the majority of stockholders confine themselves within the charter powers, a court of equity will require a strong case of mismanagement or fraud before it will interfere with the internal management of affairs of a corporation.

§22-711 (2224) **Proceedings by minority stockholders, when allowed.**—A minority stockholder may proceed in

equity in behalf of himself and other stockholders for fraud or acts ultra vires against a corporation, its officers and those participating therein, when he and they are injured thereby. But there must be shown—

1. Some action or threatened action of the directors beyond the charter powers; or,

2. Such a fraudulent transaction completed or threatened, among themselves or stockholders or others, as will result in serious injury to the company or other stockholders; or,

3. That a majority of the directors are acting in their own interest in a manner destructive of the company, or of the rights of the other stockholders; or,

4. That the majority stockholders are oppressively and illegally pursuing, in the name of the corporation, a course in violation of the rights of the stockholders, which can only be restrained by a court of equity; and it must also appear—

5. That petitioner has acted promptly; that he made an earnest effort to obtain redress at the hands of the directors and stockholders, or why it could not be done, or it was not reasonable to require it; and

6. That petitioner was a stockholder at the time of the transaction of which he complains, or that his shares have devolved on him since by operation of law.

§37-704 (4624) **Suppression of the truth.**—Suppression of a fact material to be known, and which the party is under an obligation to communicate, constitutes fraud. The obligation to communicate may arise from the confi-

dential relations of the parties or from the particular circumstances of the case.

§37-706 (4626) **Presumption; slight circumstances sometimes sufficient.**—Fraud may not be presumed, but, being in itself subtle, slight circumstances may be sufficient to carry conviction of its existence.

§37-707 (4627) **Confidential relations.**—Any relations shall be deemed confidential, arising from nature or created by law, or resulting from contracts, where one party is so situated as to exercise a controlling influence over the will, conduct, and interest of another; or where, from similar relation of mutual confidence, the law requires the utmost good faith; such as partners, principal and agent, etc.

§37-708 (4628) **Confidential relations preventing acquisition of adverse rights.**—Where by the act or consent of parties, or the act of a third person or of the law, one person is placed in such relation to another that he becomes interested for him or with him in any subject or property, he is prohibited from acquiring rights in that subject or property antagonistic to the person with whose interest he has become associated.

§37-710 (4630) **Inadequacy of consideration.**—Great inadequacy of consideration, joined with great disparity of mental ability in contracting a bargain, may justify equity in setting aside a sale or other contract.

§96-203 (4114) **Concealment amounts to fraud, when.**—Concealment of material facts may in itself amount to a fraud—

1. When direct inquiry is made, and the truth evaded.

2. When, from any reason, one party has a right to expect full communication of the facts from the other.

3. Where one party knows that the other is laboring under a delusion with respect to the property sold or the condition of the other party, and yet keeps silent. • • •

§108-429 (3767) **Profits made; accounting by trustee.**—The trustee shall not use the trust funds to his own profit. He shall be liable to account for all such profits made.